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No. 92-1293

IN THE
Supreme Court of the United States
OCTOBER TERM, 1992

NATIONWIDE CORPORATION AND
NATIONWIDE MUTUAL INSURANCE COMPANY,
Petitioners,

v.

HOWING COMPANY AND
DOUGLAS MCLELLAN,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

REPLY BRIEF OF PETITIONER

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REPLY BRIEF OF PETITIONER

Respondents' opposition tries to sidestep the fact that this Court already *granted* certiorari in this case and ordered the Sixth Circuit to reconsider its decisions in *Howing I* and *Howing II* in light of this Court's opinion in *Virginia Bankshares, Inc. v. Sandberg*, 111 S. Ct. 2749 (1991). *See Nationwide Corp. v. Howing Co.*, 112 S. Ct. 39 (1991).[1] Nor do respondents explain why the Sixth Circuit in *Howing III* failed to follow this Court's instructions on remand, and instead summarily reaffirmed its implied private right of action and materiality decisions in *Howing I* and *Howing II* without any indication of how those determinations could be reconciled with *Virginia Bankshares*.[2] Respondents also offer no explanation for the Sixth Circuit's failure in *Howing III* to follow *Virginia Bankshares*' holding that causation cannot be established where, as here, there "is no indication in the law or facts" that a "proxy solicitation resulted in any such loss." 111 S. Ct. at 2766. In so ruling, the Sixth

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[1] Respondents attempt to argue that this Court's grant of certiorari referred to the Sixth Circuit's "judgment" being vacated and thus extrapolate that only the *Howing II* decision is at issue. (Resp. Opp. at 5.) However, certiorari was granted on all issues presented. Where, as here, a certiorari order is not explicitly limited to a particular issue, certiorari is granted with respect to all the issues on which it was sought. *See Irvine v. California*, 347 U.S. 128, 129-30 (1954) ("The issues here are fixed by the petition unless we limit the grant, as frequently we do to avoid settled, frivolous or state law questions.").

[2] The Sixth Circuit dismissed this Court's previous grant of certiorari with respect to questions 1 and 2 of respondents' petition for certiorari by asserting, without any analysis, that "*Virginia Bankshares* in no way undermines our *Howing I* analysis of the private right of action issue or our *Howing II* analysis of the materiality" issue. (21a.) The Sixth Circuit overstepped its bounds in thus dismissing this Court's intervening decision as irrelevant. This Court's Order indicated that the Court found the intervening precedent "sufficiently analogous and, perhaps, decisive to compel re-examination of the case." *Henry v. City of Rock Hill*, 376 U.S. 776, 777 (1964).

Circuit has now reached decisions on three important issues—implied private rights of action, materiality and causation—that are in conflict with this Court's precedents and with the decisions of other federal courts of appeals. While respondents argue in defense of the Sixth Circuit's decisions, they cannot explain away the conflicts, and ultimately have nothing to say about the strong reasons set forth in Nationwide's Petition for this Court to grant certiorari on all three issues presented for review.

Respondents' brief opens with a statement of "facts" totally unsupported by the evidence and contrary to the District Court's explicit findings of fact left undisturbed on appeal. (Resp. Opp. at 6-8.) For example, respondents argue that the record is "still open" on the issue of whether they would have sought an appraisal remedy if Nationwide Corp. "had made the disclosures required by Rule 13e-3." (Resp. Opp. at 8.) To the contrary, the District Court's finding was that respondents consciously elected to forego their appraisal remedy under Ohio law, choosing instead to pursue their claims under the federal securities laws. (SA 641.)[3]

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[3] Similarly misplaced is respondents' assertion that Nationwide Corp.'s proxy statement failed to disclose that the merger price was approximately one times the company's book value whereas allegedly "comparable" transactions involved acquisition prices with multiples of up to four times the acquired company's book value. (Resp. Opp. at 7.) The District Court concluded that "the alleged omission of 'comparable values' was immaterial" and would have been "misleading if discussed." (116a.) The Sixth Circuit did not disturb that ruling either. (80a-81a.) Respondents also claim that First Boston and Nationwide did not determine the going concern or liquidation value of Nationwide Corp. (Resp. Opp. at 7), but the record again shows just the opposite. First Boston specifically determined that liquidation and going concern value were lower than book value, which everyone agrees was less than the merger price. (JA 251-60.) The Nationwide Corp. Evaluation Committee also agreed that all three valuations were lower than the proposed merger price. (JA 268.)

REASONS FOR GRANTING THE WRIT

Respondents seek to cover up the conflict the Sixth Circuit's decision creates with the decisions of other circuits by accusing petitioners, without explanation, of "using over-generalizations and oversimplifications . . . ." (Resp. Opp. at 8.) But petitioners specifically identified the clear and direct conflicts with decisions of the Second, Third, Tenth and D.C. Circuits with respect to the three questions presented by this certiorari petition. (*See* Petition at 6-10.) Respondents' brief does nothing to harmonize those decisions. Instead, respondents mischaracterize the Sixth Circuit's holding in an effort to make it look like there is no conflict.

Respondents assert that the Sixth Circuit's decision is not in conflict with this Court's ruling in *Virginia Bankshares* because that opinion "left open the question of whether or not loss of a state remedy may be a basis of damage causation." (Resp. Opp. at 9.) But respondents overlook the causation issue that was resolved in *Virginia Bankshares* which is dispositive here: causation cannot be established under the federal securities laws where "there is no indication in the law or facts . . . that the proxy solicitation resulted in any such loss." 111 S. Ct. at 2766. (*See* Petition at 24-27.) Moreover, the fact that the more general "lost state remedy" theory was left open in *Virginia Bankshares* only confirms that this petition presents an important question of federal law which has not been, but should be, settled by this Court. *See* Supreme Court Rule 10.1.[4]

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[4] Respondents claim *Virginia Bankshares* is inapplicable because the case "does not deal with Rule 13e-3." (Resp. Opp. at 9.) However, nothing about Rule 13e-3 entitles plaintiffs or the lower federal courts to ignore *Virginia Bankshares*, which clearly undermines the theories respondents advance here. *Virginia Bankshares* involved precisely the same type of transaction as the one at issue in this case—what this Court called a "freeze-out" merger—and thus presented precisely the same concerns. 111 S. Ct. at 2755. This Court in no way limited its holding to Section 14(a) claims involving such transactions, and petitioners do not explain why the issues of

Finally, respondents cannot be right in suggesting that only issues controlling disclosure obligations are worthy of certiorari. (Resp. Opp. at 9.) This Court has repeatedly recognized the significance of other elements of potential causes of action under the securities laws, including whether the securities laws give rise to implied damages actions, materiality and causation. It is precisely because of the broad ramifications of the Sixth Circuit's decision (*see* Petition at 7-9) that this case warrants this Court's attention.

I. THE SIXTH CIRCUIT'S IMPLICATION OF A PRIVATE RIGHT OF ACTION UNDER SECTION 13(e) CONFLICTS WITH *VIRGINIA BANKSHARES* AND OTHER DECISIONS OF THIS COURT AND OF THE SECOND AND THIRD CIRCUITS.

The Sixth Circuit's recognition of a private right of action under Section 13(e) in spite of Congressional silence is contrary to this Court's directives in *Virginia Bankshares* and prior cases, which require affirmative evidence of Congressional intent to establish implied damages actions.[5] To justify its departure, the Sixth Circuit dramatically expanded the "contemporary legal context" doctrine announced in *Cannon v. University of Chicago*, 441 U.S. 677 (1979) in a manner inconsistent with this Court's precedents and with decisions of the Second and Third Circuits holding that, notwithstanding *Cannon*, courts must apply the Supreme Court's current test rather than the one in place when the statute was passed.

Respondents' attempt to minimize *Virginia Bankshares* as a case that only addressed the "remedial scope of im-

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causation, materiality or implied damages actions should be analyzed any differently under Section 13(e). Moreover, respondents' observation that there are few reported Rule 13e-3 cases does not "suggest[]" that this case is not significant (Resp. Opp. at 9), but rather only underscores the fact that, with the exception of the Sixth Circuit, no court of appeals has recognized a private right of action under Section 13(e).

[5] *See Touche Ross & Co. v. Redington*, 442 U.S. 560 (1979); *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11 (1979).

plied remedies," not the criteria for implying private damages actions (Resp. Opp. at 10), is belied by their own description of *Virginia Bankshares* on the same page of their brief. Thus, respondents assert that *Virginia Bankshares* "loosened" the criteria for implication of private remedies (*id.* at 10 n.3)—something it obviously could not have done if it had not addressed those criteria. Moreover, respondents' erroneous attempt to distort *Virginia Bankshares* as "loosening" the standards for implying private remedies only highlights the extent to which the Sixth Circuit decision below conflicts with *Virginia Bankshares*.[6]

After raising this buckshot attack, respondents finally get to the conflict created by the Sixth Circuit with the decisions of the Second and Third Circuits on the scope of the contemporary legal context doctrine—the doctrine the Sixth Circuit relied on to find an implied right not-

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[6] Respondents also attempt to escape certiorari on whether Section 13(e) gives rise to a private damages action by insinuating that the Rule 13e-3 violation they allege somehow constituted a violation of Sections 10(b) and 14(a) of the Securities Exchange Act. But that theory has been previously rejected by the Sixth Circuit. (84a-85a.) The Sixth Circuit expressly held that no violations of Section 10(b) or 14(a) occurred in this case, and stated that since "omission of disclosure required by Rule 13e-3(e) will constitute a violation of the antifraud provisions of Sections 10(b), 13(e), and 14(a) only where the information is necessary to prevent half-truth," the violations of the rule respondents allege here "do not constitute 'fraud' under Sections 10(b) and 14(a) but should be considered as violations only of the specific rule in question." (*Id.*) More importantly, respondents' attempts to bootstrap a Rule 13(e)-3 violation into a cause of action under Sections 10(b) and 14(a) solely because the SEC referred to those sections (along with a laundry list of others) in promulgating Rule 13(e)-3 is also misguided. Other courts have expressly recognized that "[e]very rule that is promulgated under a statute providing for a private right of action will not automatically create such a right." *Angelastro v. Prudential-Bache Sec., Inc.*, 764 F.2d 939, 947-48 (3rd Cir.), *cert. denied*, 474 U.S. 935 (1985). *See also Robertson v. Dean Witter Reynolds, Inc.*, 749 F.2d 530, 537 (9th Cir. 1984) (courts should not "automatically imply a private action under every rule validly promulgated pursuant to Section 10(b)").

withstanding Congressional silence. Although respondents try to dismiss that conflict as a "difference in general methodology" (Resp. Opp. at 13), that "methodology" determines whether courts will find implied damages, and thus creates the conflict, as the decisions in *Siebert v. Conservative Party*, 724 F.2d 334 (2d Cir. 1983), *cert. denied*, 466 U.S. 980 (1984), and *American Tel. & Tel. Co. v. M/V Cape Fear*, 967 F.2d 864 (3d Cir. 1992) demonstrate. The Second Circuit held in *Siebert* that the Sixth Circuit's approach would distort *Cannon* into a rule "that the law must be frozen in time for purposes of determining whether Congress intended an implied right of action to exist." 724 F.2d at 337. Similarly, the Third Circuit held in *AT&T* that courts must apply "contemporary implication precepts to statutes enacted at a time when implication was the rule rather than the exception." 967 F.2d at 871-72. In contrast, the Sixth Circuit ruled that there was a private right of action under Rule 13e-3 because at the time that Section 13(e) was enacted, "implied rights of action were in a heyday of sorts;" therefore, Congress' silence supported the implication of such an action. (72a.) This approach lacks any limiting principle other than the date Congress enacted a statute. Thus, the fact that the Sixth Circuit did not explicitly state that it was declaring a private right of action for every statute enacted between 1917 and 1975 matters not; its application of the contemporary legal context test leads to that result. Accordingly, Nationwide's Petition presents a question of enormous importance.

II. *VIRGINIA BANKSHARES* MAKES CLEAR THAT THE SIXTH CIRCUIT'S APPLICATION OF A PRESUMPTION OF MATERIALITY CONFLICTS WITH THIS COURT'S DECISION IN *TSC INDUSTRIES* AND DECISIONS OF OTHER FEDERAL COURTS OF APPEALS.

The Sixth Circuit's holding that materiality must be *presumed* in cases involving going-private mergers is contrary to decisions of this Court and the federal courts of appeals, as reinforced by *Virginia Bankshares*, where

this Court applied the standard of materiality established in *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 449 (1976) in the going-private merger context. Respondents continue their bizarre interpretation of *Virginia Bankshares* by arguing that "*Virginia Bankshares* gives a more expansive reading to the concept of materiality" than *TSC* and thereby authorizes the Sixth Circuit's *presumption* of materiality. (Resp. Opp. at 15.) This Court needs to take this case to prevent this impermissible departure from the *TSC* standard of materiality.

Contrary to respondents' creative theorizing, this Court in *Virginia Bankshares* reaffirmed that liability under the securities laws, including cases involving going-private mergers, must be determined by the *TSC* standard. Respondents focus on the fact that the Court noted that directors' statements of reasons, opinions or beliefs as to the fairness of a transaction are potentially actionable under the securities laws. (Resp. Opp. at 15.) But this attempt to equate Nationwide Corp.'s disclosure with the directors' interests in *Virginia Bankshares* relates to issues long ago resolved against respondents.

In defense of the Sixth Circuit's substitution of its own "presumption of materiality" for this Court's established *TSC* standard, respondents assert that the Sixth Circuit's "presumption" is somehow "consistent" with *TSC*, or alternatively, that *TSC* is irrelevant because it was not decided under Section 13(e). (Resp. Opp. at 15-17.) Neither contention has any merit.

First, despite respondents' effort to reconcile the Sixth Circuit's "heightened" materiality standard with *TSC*, the "presumption of materiality" respondents now seek to trivialize is both broad and pernicious. Under respondents' formulation, materiality is automatically presumed when the SEC mandates disclosure of "specific items of information." (Resp. Opp. at 15.) Tellingly, respondents offer no indication of how any issuer of a proxy statement can overcome such a "presumption of materiality." Indeed, respondents affirmatively argue for this very result, contending that information required by the SEC is "pre-

sumptively material for purposes of defeating a motion for summary judgment." (Resp. Opp. at 15.) But for that presumption, respondents would have lost as a matter of law under *TSC*, as the District Court concluded. (52a-53a.) Only the Sixth Circuit's presumption led it to deem information material that other courts of appeals, correctly applying *TSC*, have held to be immaterial. (*See* Petition at 21-22.)

Second, the fact that this case involves Section 13(e) does not afford the Sixth Circuit a license to depart from *TSC*. This Court and other courts of appeals have applied *TSC* to judge materiality under *all* of the securities statutes. In fact, the D.C. Circuit so interpreted *TSC* in applying it to Section 13(e) in *Berg v. First American Bankshares, Inc.*, 796 F.2d 489, 495, 502 (D.C. Cir. 1986). Even absent this conflict, respondents offer no persuasive rationale—indeed, no rationale at all—for believing that a different "heightened" standard should apply to cases brought under Section 13(e) or that any "presumption of materiality" is appropriate in this context. Their only justification—that a different standard is required if a proxy statement involves a going-private merger or the omission of information required by an SEC schedule or regulation—conflicts with this Court's decisions in *Basic Inc. v. Levinson*, 485 U.S. 224 (1988), and *Virginia Bankshares* as well as other appellate decisions discussed in Nationwide's Petition, including *United States v. Bilzerian*, 926 F.2d 1285, 1298-99 (2d Cir.), *cert. denied*, 112 S. Ct. 63 (1991), and *Pavlidis v. New England Patriots Football Club, Inc.*, 737 F.2d 1227, 1231 (1st Cir. 1984).

III. THE SIXTH CIRCUIT'S INTERPRETATION OF THE LOST STATE REMEDY THEORY IS IN CONFLICT WITH THIS COURT'S DECISION AND THE DECISIONS OF THE THIRD AND TENTH CIRCUITS.

The Sixth Circuit's novel adoption and application of the "lost state remedies" theory of causation conflicts with this Court's decision in *Virginia Bankshares* and

decisions of other courts of appeals. Respondents attempt to explain away the conflict with the Third and Tenth Circuits' decisions in *Scattergood v. Perelman*, 945 F.2d 618 (3d Cir. 1991), and *Boone v. Carlsbad Bancorporation, Inc.*, 972 F.2d 1545 (10th Cir. 1992), by noting language in those decisions that *Virginia Bankshares* never reached the ultimate question of whether there are any circumstances under which a plaintiff can establish materiality under a lost state remedy theory. (Resp. Opp. at 19.) True enough, but respondents miss the point. Whatever the resolution of that ultimate question, this Court made clear in *Virginia Bankshares* that a lost state remedy theory cannot be used to establish materiality where the causation claim rests on speculation. 111 S. Ct. at 2765.

In contrast to the Sixth Circuit's decision in this case, the Tenth Circuit correctly applied *Virginia Bankshares* in *Boone* to bar a claim identical to respondents' where it would be "mere speculation to assume that plaintiffs *would* have sought an injunction" had the additional information been provided them. 972 F.2d at 1559 (emphasis in original). Thus, the Tenth Circuit affirmed summary judgment against a group of plaintiffs who had failed to present "evidentiary materials sufficient to establish a factual issue on causation stemming from an allegedly lost state remedy." *Id.* at 1558. Similarly, in *Scattergood*, the Third Circuit ruled that no claim for loss of state remedies can be maintained under the federal securities laws without proof that the plaintiffs lost "an opportunity under state law to enjoin a merger." 945 F.2d at 626 n.4.[7]

In sharp contrast to the Third and Tenth Circuits, the Sixth Circuit cited absolutely no evidence in *Howing III*,

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[7] Respondents argue that *Howing III* "is fully consistent" with *Wilson v. Great American Indus., Inc.*, 979 F.2d 924 (2d Cir. 1992). (Resp. Opp. at 20.) Even if true, this observation does nothing to dispense with the conflict with *Scattergood* and *Boone*. In fact, it would only confirm the circuit split on the issue.

merely speculating that respondents' decisions "with respect to appraisal might well have been different had they received the full and fair disclosure to which they were entitled." (19a.) Such speculation is insufficient. Under *Virginia Bankshares*, causation is lacking where "there is no indication in the law or facts . . . that the proxy solicitation resulted in" lost state remedies. 111 S. Ct. at 2766.

Respondents' assertion that there is no record of "what they would have done had Petitioners made the full disclosures required by Rule 13e-3" (Resp. Opp. at 20) is completely inaccurate. The uncontroverted evidence showed that plaintiffs were fully informed of their appraisal rights and provided with potential reasons for exercising those rights, which were fully preserved under Ohio law. (JA 93, 97-98, 246.) The evidence also showed that respondents and their counsel admitted that plaintiffs consciously elected not to pursue their appraisal rights, choosing instead to pursue their claim under the federal securities laws, and the District Court so found. (SA 623, 627-28, 630-31, 633-36, 641.) The Sixth Circuit left these findings undisturbed on appeal. Moreover, contrary to their assertions, respondents had every opportunity "to submit affidavits addressed to what they would have done." (Resp. Opp. at 20.) Having twice been faced with dispositive motions for summary judgment (both granted by the District Court), respondents were obliged to come forward with sufficient evidence to establish the elements of their claims. *See Celotex Corp. v. Catrett*, 477 U.S. 317, 332 (1986). Accordingly, there is no basis for any finding except that the proxy violation respondents assert caused them no damage cognizable by the federal securities laws.

CONCLUSION

For the foregoing reasons, and for those stated in the Petition, a writ of certiorari should be granted.

Respectfully submitted,

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